

**REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND  
THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE  
INFORMATION OF THE THABO MOFUTSANYANA DISTRICT MUNICIPALITY FOR  
THE YEAR ENDED 30 JUNE 2009**

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I was engaged to audit the accompanying financial statements of the Thabo Mofutsanyana District Municipality which comprise the balance sheet as at 30 June 2009, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] to [xx].

**The accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation of these financial statements in accordance with the entity-specific basis of accounting, as set out in accounting policy note 1 and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

**The Auditor-General's responsibility**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

**Basis for disclaimer of opinion**

**Fixed assets**

4. The comparative figures regarding fixed assets as at 30 June 2008 as disclosed in note 2 to the financial statements have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures have been restated from R5 587 744 to R nil. Sufficient appropriate audit evidence could not be obtained for the restatement of R5 587 744 as management could not substantiate the restatement. This restatement was also not disclosed in the financial statements. I was unable to confirm by alternative means the occurrence and accuracy of the adjustments to the comparative figures for fixed assets as the municipality's records did not permit the application of alternative procedures.

5. Sufficient appropriate audit evidence as to the completeness, existence, valuation, and rights regarding fixed assets as disclosed in note 2 to the financial statements could not be obtained due to the following matters:
- (a) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R1 653 331 recognised in fixed assets as management could not provide journal vouchers or supporting documentation. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
  - (b) Fixed assets to the amount of R460 116 were recognised at fair value in the fixed asset register. Sufficient appropriate audit evidence could not be obtained regarding the values of these fixed assets as the supporting documentation could not be submitted by management. I was unable to confirm by alternative means the valuation of these fixed assets as the municipality's records did not permit the application of alternative procedures.
  - (c) Fixed assets to the amount of R722 255 (2008: R115 158) could not be physically verified. I was unable to confirm by alternative means the existence of these fixed assets.
  - (d) Fixed assets to the amount of R120 635 that were disposed of during the year could not be traced to the supporting documentation to substantiate the disposal of the assets as the auctioneer's report did not contain appropriate information. I was unable to confirm by alternative means the existence and valuation of these fixed asset disposals as the municipality's records did not permit the application of alternative procedures.
  - (e) The mayoral vehicle purchased for R620 000 was not capitalised for the year ended 30 June 2008. The fixed assets are thus understated by R620 000 and operating expenditure for the previous is overstated by the same amount.
  - (f) The capital expenditure and the assets written off, transferred or disposed of as disclosed in note 2 of the financial statements, amounting to R552 866 did not include capital expenditure for general services amounting to R1 082 556. The fixed asset additions and capital expenditure for general services are therefore both understated by R1 082 556.

#### **Investments**

6. Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R48 227 584 recognised in investments, as disclosed in note 3 to the financial statements, for the year ended 30 June 2008 as management could not submit the journal vouchers. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
7. Investments amounting to R16 271 774 according to note 3 to the financial statements exceeded the amount confirmed via bank confirmations by R540 323. I was further unable to identify the other account that is misstated as sufficient appropriate audit evidence could not be presented and alternative procedures could not be performed due to any listings available for suspense accounts.

### **Cash and bank**

8. The comparative figures for cash and bank as at 30 June 2008 as disclosed in note 5 to the financial statements have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures were restated from R15 585 811 to R12 801 078. Sufficient appropriate audit evidence could not be obtained to confirm the occurrence and accuracy of the restatement of R2 784 733 as management could not substantiate the restatement. This restatement was also not disclosed in the financial statements. I was unable to confirm by alternative means the valuation of cash and bank as at 30 June 2008 as the municipality's records did not permit the application of alternative procedures.
9. Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R14 564 500, recognised in cash and bank during the year under review, as management could not submit the required journal vouchers. The municipality's records did not permit the application of alternative audit procedures and therefore sufficient appropriate audit evidence for the completeness, valuation and existence of cash and bank amounting to R1 230 539 (2008: R15 585 811), as disclosed in note 5 to the financial statements could not be obtained.
10. A bank account with a balance of R600 439 was identified on the bank confirmation as at 30 June 2009, which is not included in cash and bank. Bank reconciliations were also not performed during the year. Cash and bank are therefore understated by R600 439. I was unable to confirm the total extent of income, expenditure, assets or liabilities that might result from this unrecognised bank account as sufficient appropriate audit evidence could not be presented and alternative procedures could not be performed as the bank statements for this bank account could not be provided by the municipality.

### **Debtors**

11. The comparative figures regarding debtors as at 30 June 2008 as disclosed in note 4 to the financial statements have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures have been restated from R64 070 549 to R5 352 431. Sufficient appropriate audit evidence could not be obtained for the restatement of R58 718 118 as management could not substantiate the restatement and it was not disclosed in the financial statements. I was unable to confirm by alternative means the occurrence and accuracy of these restatements as the municipality's records did not permit the application of alternative procedures.
12. The completeness, existence and valuation of debtors amounting to R13 816 160 (2008: R5 352 431), as disclosed in note 4 to the financial statements, could not be confirmed due to the following:

- (a) Sufficient appropriate audit evidence could not be obtained in respect of the arrear levy debtors amounting to R34 155 283 (2008: R35 290 087) as debtor lists were not maintained by the municipality. The outstanding gross arrear levy debtors also did not agree with the list of debtors obtained from the attorneys. There was a difference of R5 244 179 for the current year which could not be explained by management. Due to the lack of sufficient appropriate audit evidence in this regard, I was unable to perform alternative procedures to obtain audit assurance as to the existence, valuation, and rights and obligations of the arrear levy debtors as the municipality's records did not permit the application of alternative procedures.
- (b) Suspense accounts were not cleared regularly and were not cleared at 30 June 2009. Supporting documentation could also not be obtained to substantiate debtors to the amount of R7 671 600 as no reconciliations have been done during the year. Owing to the lack of evidence, I was unable to confirm by alternative means the existence and valuation of these debtors as no listings for suspense accounts were available.
- (c) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R1 586 768 (2008: R848 669) recognised in debtors during the year under review as management could not submit the journal vouchers or supporting documentation. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
- (d) The movements in the arrear levy debtors amounted to R1 134 804 (2008: R335 864). The schedules from the attorneys recovering the arrear levies could not be obtained. I was unable to confirm by alternative means the existence, valuation and classification of the arrear levy debtors recovered as the municipality's records did not permit the application of alternative procedures.

#### **Accumulated surplus**

- 13. The comparative figures for accumulated surplus as at 30 June 2008 as disclosed in note 1.1 to the financial statements have been restated as a result of errors discovered during the financial year. The accumulated surplus as at 30 June 2008 has been restated from R66 247 004 to R9 464 442. Sufficient appropriate audit evidence could not be obtained to confirm the occurrence and accuracy of the restatement of R56 782 562. This restatement was also not disclosed in the financial statements. I was unable to confirm by alternative means the valuation of the accumulated surplus as at 30 June 2008 as the municipality's records did not permit the application of alternative procedures.
- 14. Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R6 753 828 processed for 30 June 2008 as no journal vouchers could be presented by management to the accumulated surplus as disclosed in note 1.1 in the current year. I was unable to confirm by alternative means the occurrence and accuracy of these journals recognised in the accumulated surplus as the municipality's records did not permit the application of alternative procedures.

## Creditors

15. Creditors for the previous year as disclosed in note 7 to the financial statements have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures were restated from R41 587 118 to R36 832 333. Sufficient appropriate audit evidence could not be obtained for the restatement of R4 754 785 as management could not substantiate the restatement and it was not disclosed in the financial statements. I was unable to confirm by alternative means the occurrence and accuracy of the adjustments to the comparative figures for creditors as the municipality's records did not permit the application of alternative procedures.
16. The completeness, existence, valuation, and rights and obligations of creditors amounting to R32 594 699 (2008: R36 832 333) as disclosed in note 7 to the financial statements could not be confirmed due to the following:
  - (a) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R6 679 112 for the previous year recognised in creditors as management could not submit the journal vouchers or supporting documentation. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
  - (b) No creditor reconciliations were performed at year-end. Suspense accounts were not cleared regularly and were not cleared at 30 June 2009. Sufficient appropriate audit evidence could not be obtained to substantiate creditors to the amount of R31 111 629 (2008: R30 964 814) as management could not provide us with creditor listings. I was unable to confirm by alternative means the existence, rights and obligations, and valuation of creditors.
  - (c) Sufficient appropriate audit evidence could not be obtained in respect of creditor payments to the amount of R9 146 979 for the previous year as no supporting documentation was attached to the payment vouchers or the payment vouchers could not be submitted for audit purposes. Owing to the lack of evidence, I was unable to confirm by alternative means the occurrence or accuracy of these creditor payments as the municipality's records did not permit the application of alternative procedures.
  - (d) Payments amounting to R841 451 were incorrectly allocated to creditors instead of the expenditure accounts. Creditors and expenditure are therefore understated by R841 451.
  - (e) Creditors and expenditure were understated by R472 037 for the previous year as the supporting invoice amounts exceeded the amounts recognised in creditors and expenditure.



## **Provisions**

17. The completeness, valuation, and obligations of provisions amounting to R2 790 741 (2008: R3 090 361) as disclosed in note 6 to the financial statements could not be confirmed due to the following:
  - (a) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R848 503 recognised in provisions during the financial year ended 30 June 2008 as management could not substantiate the restatement. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
  - (b) Sufficient appropriate audit evidence could not be obtained for leave taken by employees to the amount of R94 760 as no leave forms were available in the leave files and the municipality did not have adequate leave registers. I was unable to confirm by alternative means the occurrence and accuracy of the leave taken and the resulting influence on the provision for leave.
18. Provisions amounting to R2 790 741 (2008: R3 090 361) as disclosed in note 6 to the financial statements are not reasonably stated. Calculation errors were identified in the provision for leave pay amounting to R1 721 128, as disclosed in note 6 to the financial statements. The calculation errors identified amounted to R245 273. Provisions and employee cost are therefore overstated by this amount.

## **Revenue**

19. The comparative figures regarding revenue for the financial year ended 30 June 2008 as disclosed in the income statement have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures have been restated from R113 978 081 to R75 382 339. Sufficient appropriate audit evidence could not be obtained for the restatement of R38 595 742 as management could not substantiate the restatement. This restatement was also not disclosed in the financial statements. I was unable to confirm the occurrence and accuracy of the restatement as the municipality's records did not permit the application of alternative procedures.
20. The completeness, accuracy and occurrence of revenue amounting to R70 909 471 (2008: R75 382 339) according to the income statement could not be confirmed due to the following:
  - (a) Receipts on the direct deposit register amounting to R416 450 for the year ended 30 June 2008 could not be traced to the bank statements. I was unable to confirm by alternative means the existence and valuation of these arrear levy debtors recovered as the municipality's records did not permit the application of alternative procedures.
  - (b) The interest received from investments amounting to R4 950 901 as disclosed in note 10 of the financial statements for the year ended 30 June 2008 did not agree with the interest received totalling R3 706 302, as disclosed in note 3 to the financial statements, relating to investments. The difference amounted to R1 244 599. Sufficient appropriate audit

evidence could not be obtained for this difference. I was unable to confirm by alternative means the accuracy and classification of interest received.

- (c) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R2 000 000 recognised in revenue during the year under review as management could not provide the supporting documentation. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.
21. Direct deposits amounting to R82 497 were confirmed on the bank statements for the year ended 30 June 2008 but could not be traced to the general ledger accounts. Arrear levy debtors were therefore overstated by this amount and cash and bank understated by the same amount for the previous year.

#### **Fruitless and wasteful expenditure**

22. Section 1 of the MFMA states that fruitless and wasteful expenditure means expenditure that was made in vain and would have been avoided had reasonable care been exercised. Due to the fact that the municipality did not disclose in the annual financial statements the fruitless and wasteful expenditure as detailed below, as required by section 125(2)(d) of the MFMA, the fruitless and wasteful expenditure is understated:
- (a) Lump sum payments amounting to R231 856 had to be made during the year under review to temporary employees due to unfair dismissals.
  - (b) The arrear levy debtors recovered during the year under review amounted to R1 134 804 and the legal expenses paid to recover these levies amounted to R4 535 493. The difference of R3 400 689 is deemed as fruitless expenditure as the benefits did not exceed the expenditure.

#### **Unauthorised expenditure**

23. Section 1 of the MFMA defines unauthorised expenditure as any expenditure incurred by a municipality otherwise than in accordance with sections 15 or 11(3) of the act, and includes overspending of the total amount appropriated in the municipality's approved budget. The actual expenditure for special projects amounted to R27 470 909 and the budget allocated for these projects were R20 733 875, thus resulting in unauthorised expenditure of R6 737 034. Contrary to section 125(2)(d) of the MFMA, the above unauthorised expenditure to the amount of R6 737 034 was also not disclosed in the financial statements as unauthorised expenditure. Unauthorised expenditure in the notes to the financial statements is therefore understated by R6 737 034.

#### **Employee cost**

24. The councillors' remuneration as disclosed in note 8 to the financial statements does not include the municipality's contributions amounting to R2 703 967. This amount was incorrectly included in general expenditure. The councillors' remuneration is therefore understated and general expenditure overstated by R2 703 967.

25. Sufficient appropriate audit evidence as to the occurrence, accuracy and classification of employee cost amounting to R21 173 657 (2008: R23 323 083) and councillors' remuneration amounting to R3 966 788 (2008: R3 895 646) as disclosed in appendix C to the financial statements could not be obtained due to the following:
- (a) The salaries and councillors' allowances disclosed in appendix C to the financial statements do not agree with the salaries according to the VIP system. The financial statement figure is R883 601 less than the amount according to the VIP system. Furthermore, the amount for salaries and councillors' allowances according to the VIP system is R2 391 896 less than the amount according to the general ledger. Monthly reconciliations were also not performed between the VIP system and the general ledger. I was unable to perform any alternative procedures.
  - (b) Differences amounting to R115 022 (2008: R823 335) were identified between the information on the VIP system and the actual payments made to third parties. Sufficient appropriate audit evidence could not be obtained to explain these differences. I was unable to confirm by alternative means the reasons for the differences identified as the municipality's records did not permit the application of alternative procedures.
  - (c) Section 125(1)(c) of the MFMA states that the notes to the financial statements of a municipality must include total amounts paid in taxes, levies, duties, pension and medical aid contributions, and whether any amounts were outstanding as at the end of the financial year. The PAYE and UIF payments to the amount of R4 090 420 as well as pension and medical aid fund payments amounting to R3 840 277 were not separately disclosed in the notes to the financial statements.
26. The municipality did not comply with the supply chain management policy as required by section 65(i) of the MFMA for expenses amounting to R57 337 006 (2008: R17 798 339). No evidence could be submitted to confirm that payment vouchers were authorised, tenders were invited, tax clearance certificates were obtained and written quotations were obtained as required by the supply chain management policy. This expenditure is regarded as irregular in terms of the MFMA and irregular expenditure is thus understated by this amount. Contrary to section 125(2)(d) of the MFMA, the above was also not disclosed in the financial statements as irregular expenditure.
27. In terms of section 1 of the MFMA, irregular expenditure is defined as expenditure incurred by a municipality in contravention of, or that is not in accordance with, a requirement of the Public Office-Bearers Act, 1998 (Act No. 20 of 1998). The remuneration packages disclosed in note 8 to the financial statements for the year ended 30 June 2008 regarding the executive mayor's allowance, the chief whip's allowance and the mayoral committee member's allowance exceeded the remuneration packages as approved in *Government Gazette* No. 30600, dated 18 December 2007 and issued under the Public Office-Bearers Act, 1998 (Act No. 20 of 1998) by R532 289 and are thus considered irregular in terms of the MFMA. The irregular expenditure as at 30 June 2008 is therefore understated by R532 289. Contrary to section 125(2)(d) of the MFMA, the above was also not disclosed in the financial statements as irregular expenditure.



28. I could not be provided with sufficient, appropriate audit evidence that management has properly identified, investigated and recorded all irregular expenditure transactions during the year under review. There were no satisfactorily alternative audit procedures that I could perform to confirm the completeness of irregular expenditure as disclosed in the financial statements.

### **Expenditure**

29. The comparative figures for operating expenditure for the year ended 30 June 2008 as disclosed in the income statement have been restated as a result of errors discovered during the 2008-09 financial year. The comparative figures were restated from R105 888 550 to R123 776 452. Sufficient appropriate audit evidence could not be obtained for the restatement of R17 887 902 as management could not substantiate the restatement. This restatement was also not disclosed in the financial statements. I was unable to confirm by alternative means the occurrence and accuracy of the adjustments to the comparative figures for operating expenditure as the municipality's records did not permit the application of alternative procedures.
30. Sufficient appropriate audit evidence as to the occurrence, accuracy and classification of operating expenditure amounting to R90 920 609 (2008: R123 776 452) as disclosed in the income statement could not be obtained due to the following:
- (a) Legal fees paid to attorneys according to the reconciliation received from the attorneys amounting to R380 333 could not be identified in the municipality's bank statements or general ledger for 30 June 2008. I was unable to confirm by alternative means the occurrence, completeness and accuracy of these payments as the municipality's records did not permit the application of alternative procedures.
  - (b) Sufficient appropriate audit evidence could not be obtained in respect of payments to the amount of R20 755 176 (2008: R14 558 999) as no supporting documentation was attached to the payment vouchers or the payment vouchers could not be submitted for audit purposes. Owing to the lack of evidence, I was unable to confirm by alternative means the occurrence and accuracy of these expenditure.
  - (c) Various expense transactions were identified that had been duplicated in the general ledger accounts. All these transactions amounting to R2 470 233 were recognised through the creditors suspense account in the general ledger. Sufficient appropriate audit evidence could only be provided for one payment of each transaction that was identified to have been duplicated. Expenditure is thus overstated by R 2 470 233, creditors by R2 550 807 and debtors by R80 574.
  - (d) Sufficient appropriate audit evidence could not be obtained in respect of journal entries amounting to a total value of R227 174 (2008: R1 662 611) recognised in operating expenditure as the journal vouchers or supporting documentation could not be submitted by management. I was unable to confirm by alternative means the occurrence and accuracy of these journals as the municipality's records did not permit the application of alternative procedures.

- (e) Various expense transactions were identified that had been duplicated in the general ledger accounts for 30 June 2006. All of these transactions amounting to R1 846 446 were recognised through the main bank account in the general ledger. Sufficient appropriate audit evidence could not be provided for these payments as well as proof that these payments were actually made twice out of the bank account. I was unable to confirm by alternative means the occurrence and accuracy of the payments due to the payments being processed in batches.
- (f) Expenditure recognised in the general ledger exceeded the supporting invoices by R1 612 893. Sufficient appropriate audit evidence could not be obtained for this difference and the accounting records of the municipality did not allow me to perform alternative procedures.
- (g) Input tax amounting to R734 392 (2008: R1 118 346) was incorrectly recognised as expenditure due to invoices being incorrectly captured on the accounting system. Expenditure and VAT receivable are therefore overstated by this amount.

#### **Value-added tax**

- 31. Sufficient appropriate audit evidence as to the existence, valuation and completeness of value-added tax (VAT), included in note 5 to the financial statements, could not be obtained as no monthly or year-end reconciliations have been performed between the general ledger and the VAT returns, with the result that the VAT returns did not balance with the general ledger. The difference between the VAT returns and the general ledger amounted to R3 041 511 (2008: R805 807). Sufficient appropriate audit evidence could not be obtained for the differences. I was unable to confirm by alternative means the valuation of the VAT receivable.

#### **Cash flow statement**

- 32. The cash flow statement for the year ended 30 June 2008 contains several calculation errors. The cash generated by activities is understated by R2 332 478, interest received is understated by R5 546, working capital changes are overstated by R2 337 035 and increase in cash and bank is overstated by R990. The appropriations charged against income amounting to R2 834 684 did not cast correctly in the cash flow statement. The recalculated amount was R32 196 504 and therefore the appropriations were understated by R35 031 188. The cash flow statement is therefore not accurate.
- 33. The decrease in working capital changes to the amount of R63 682 301 for the year ended 30 June 2008 as per the cash flow statement does not agree with the amount in note 13 to the financial statements. The difference amounted to R43 112 969. The cash flow statement and the notes in the financial statements are therefore not accurate.
- 34. The cash flow statement for the year ended 30 June 2009 contains several calculation errors. The cash generated by activities is overstated by R1 260 683, increase in cash investments is overstated by R1 309 170, interest received understated by R2 108 and working capital changes is understated by R2 571 962. The cash flow statement is therefore not accurate.

35. The increase in working capital changes to the amount of R10 129 401 disclosed in the cash flow statement for the year ended 30 June 2009 did not agree with the amount in note 13 to the financial statements. The difference amounted to R4 550 913. The cash flow statement and the notes in the financial statements are therefore not accurate.

#### **Contingent liabilities**

36. Sufficient appropriate audit evidence could not be obtained to confirm the accuracy of housing guarantees amounting to R1 634 000 as disclosed in note 18.1 to the financial statements due to the guarantee files not provided for audit purposes. Sufficient appropriate audit evidence could also not be obtained as assurance that all contingent liabilities have been disclosed. Owing to the lack of sufficient appropriate audit evidence, I was not able to confirm by alternative means the accuracy and completeness of contingent liabilities.

#### **Commitments**

37. Sufficient appropriate audit evidence could not be obtained as assurance that all commitments have been disclosed. Owing to the lack of sufficient appropriate audit evidence, I was not able to confirm by alternative means the completeness of commitments as the schedule of commitments was not maintained.

#### **Going concern**

38. According to the stipulations in section 138 of the MFMA, the municipality can be regarded as a municipality with serious financial problems as the following indicators were identified:

- The municipality had an operating deficit in excess of 5% of revenue in the most recent financial year.
- The Auditor-General had issued a disclaimer in the previous year due to inadequacies in the financial statements and records of the municipality.

The following indicators were identified during the review of the financial statements for the year under review:

- Cash and cash investments decreased significantly.
- The current ratio of current assets in relation to the current liabilities is 0.35:1, which is below the norm of 2:1.
- The funds and reserves at year-end are R4 066 968 in debit, which states that the total liabilities of the municipality exceeded the total assets and the municipality is thus in an insolvent position.
- The municipality had a deficit of R20 011 138 for the financial year under review, which constitutes 28% of revenue for the year.
- The creditor payment period increased from 139 days in 2008 to 227 days in the financial year under review.

The above findings indicate the existence of a material uncertainty of the municipality's ability to continue as a going concern in the near future. The financial statements do not disclose this matter of uncertainty.

The municipality was also placed under administration in terms of section 139(1)(b) of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) due to the complete breakdown of the administration of the municipality with effect from 6 November 2009.

#### **Disclaimer of opinion**

39. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

#### **Emphasis of matters**

40. I draw attention to the following matters on which I do not express a disclaimer of opinion:

#### **Basis of accounting and amendments to the applicable basis of accounting**

41. The entity's policy is to prepare financial statements on the entity-specific basis of accounting, as set out in accounting policy note 1.1 to the financial statements.

#### **Other matters**

42. I draw attention to the following matters:

#### **Unaudited supplementary schedules**

43. The appendices set out on pages XX to XX do not form part of the financial statements and are presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

#### **Non-compliance with applicable legislation**

##### **Municipal Finance Management Act**

44. Contrary to section 65(2)(e) of the MFMA, payments amounting to R1 678 298 were not made within 30 days of receipt of the invoice.
45. The municipality did not table the annual report within seven months after year-end as required by section 127(2) of the MFMA. In addition, no written explanation setting out the reasons for the delay was submitted to the council as required by section 127(3) of the MFMA.
46. The annual report for the 2007-08 financial year did not include an assessment of arrears on municipal taxes and service charges or an assessment of the municipality's performance against the measurable performance objectives for revenue collection as required by section 121(3) of the MFMA.
47. No evidence could be obtained that the mayor tabled the annual budget 90 days before the start of the financial year for 2008-09 as required by section 16 of the MFMA.
48. The process plan for the 2008-09 budget preparation was not tabled to the council within the prescribed period of 10 months as required by section 21 of the MFMA. A budget-related policy was also not adopted by the council.

49. The annual budget for the 2008-09 financial year was not accompanied by all the information required by section 17(3) of the MFMA.
50. Although the municipality faces serious financial and cash flow problems, I could not determine whether the mayor had responded promptly to and initiated remedial or corrective steps proposed by the accounting officer to deal with such problems as required by section 54 of the MFMA.
51. No evidence could be obtained that the accounting officer reported to the council any impending shortfalls in budgeted revenue and overspending of the municipality's budget as required by section 70(1) of the MFMA.
52. Contrary to section 71 of the MFMA five monthly budget statement reports were submitted late to the National Treasury.

### **Municipal Systems Act**

53. Contrary to section 7 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA), not all councillors submitted signed declarations of interest.

### **Governance framework**

54. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

### **Internal control deficiencies**

55. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the district municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control (the number listed per component can be followed with the legend below the table.) In some instances deficiencies exist in more than one internal control component.

| Par. No.       | Basis for disclaimer of opinion    | CE | RA   | CA             | IC | M    |
|----------------|------------------------------------|----|------|----------------|----|------|
| 4, 5           | Accumulated surplus                |    |      | 3, 4           |    |      |
| 6, 7, 8        | Cash and bank                      |    |      | 3, 4, 5        |    |      |
| 9, 10, 11, 12  | Cash flow statement                | 5  |      |                |    | 1    |
| 13             | Contingent liabilities             | 6  |      |                |    |      |
| 14             | Commitments                        | 6  |      |                |    |      |
| 15, 16, 17, 18 | Employee cost                      | 5  |      | 3              |    | 1    |
| 19, 20         | Irregular expenditure              | 5  | 2, 4 | 3, 4, 5, 8, 11 |    | 1    |
| 21             | Fruitless and wasteful expenditure | 5  |      |                |    |      |
| 23, 24         | Investments                        |    |      | 3              |    |      |
| 25, 26, 27     | Operating expenditure              | 5  |      | 3, 4, 11       |    | 1, 2 |



|            |                          |   |  |               |   |   |
|------------|--------------------------|---|--|---------------|---|---|
| 28         | Unauthorised expenditure | 5 |  |               |   |   |
| 29, 30, 31 | Creditors                | 7 |  | 2, 3, 5, 6, 9 |   | 1 |
| 32, 33, 34 | Fixed assets             | 5 |  | 3, 4, 5       |   | 1 |
| 35, 36     | Debtors                  | 5 |  | 3, 5          | 1 | 1 |
| 37, 38, 39 | Revenue                  | 5 |  | 3, 4, 9       |   |   |
| 40, 41     | VAT                      |   |  | 3, 5          |   | 1 |
| 42, 43     | Provisions               | 5 |  | 3             |   |   |

### Overall reflections on the governance framework based on internal control deficiencies

56. The accounting officer and the chief financial officer were not operating as a team to achieve the municipality's overall set objectives.
57. The chief financial officer did not sufficiently monitor the recording and reconciliation of the financial records. Sufficient control measures were not developed by the chief financial officer in conjunction with the support team, to address all the qualifications reported in the prior years as identified in the action plan. Draft policies and procedures were only drawn up during the current financial year.
58. The accounting officer did not prioritise and take appropriate actions to address the lack of discipline in the supply chain management directorate, and as a result non-compliance with applicable legislation occurred. This resulted in irregular, fruitless and wasteful, as well as unauthorised expenditure.

| Legend  |   |
|---|---|
| CE = Control environment  |   |
| The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.       | 1 |
| Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.                  | 2 |
| Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.                                  | 3 |
| Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.                                  | 4 |
| The accounting officer/accounting authority does not exercise oversight responsibility over financial reporting and internal control.                     | 5 |
| Management's philosophy and operating style do not promote effective control over financial reporting.  | 6 |
| The entity does not have individuals competent in financial reporting and related matters.  | 7 |
| RA = Risk assessment  |   |
| Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.                        | 1 |
| The entity does not identify risks to the achievement of financial reporting objectives.  | 2 |
| The entity does not analyse the likelihood and impact of the risks identified.  | 3 |
| The entity does not determine a risk strategy/action plan to manage identified risks.   | 4 |
| The potential for material misstatement due to fraud is not considered.   | 5 |
| CA = Control activities   |   |
| There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.  | 1 |
| General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.          | 2 |
| Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed. | 3 |
| Actions are not taken to address risks to the achievement of financial reporting objectives.  | 4 |
| Control activities are not selected and developed to mitigate risks over financial reporting.   | 5 |
| Policies and procedures related to financial reporting are not established and communicated.  | 6 |
| Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.                             | 7 |

|  |   |
|--|---|
| <b>IC = Information and communication</b>  |   |
| Pertinent information is not identified and captured in a form and time frame to support financial reporting.                                    | 1 |
| Information required to implement internal control is not available to personnel to enable internal control responsibilities.                    | 2 |
| Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.        | 3 |
| <b>M = Monitoring</b>  |   |
| Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting. | 1 |
| Neither reviews by internal audit or the audit committee nor self-assessments are evident.   | 2 |
| Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.                 | 3 |

### Key governance responsibilities

59. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

| No.   | Matter  | Y | N |
|---|---|---|---|
| <b>Clear trail of supporting documentation that is easily available and provided in a timely manner</b>     |   |   |   |
| 1.  | No significant difficulties were experienced during the audit concerning delays or the availability of requested information. |   | X |
| <b>Quality of financial statements and related management information</b>                                   |   |   |   |
| 2.  | The financial statements were not subject to any material amendments resulting from the audit.                                |   | X |
| 3.  | The annual report was submitted for consideration prior to the tabling of the auditor's report.                               | X |   |
| <b>Timeliness of financial statements and management information</b>  |   |   |   |
| 4.  | The annual financial statements were submitted for auditing as per the legislated deadlines in section 126 of the MFMA.       | X |   |
| <b>Availability of key officials during audit</b>   |   |   |   |
| 5.  | Key officials were available throughout the audit process.  |   | X |
| <b>Development and compliance with risk management, effective internal control and governance practices</b> |   |   |   |
| 6.  | Audit committee   |   |   |
|   | • The district municipality had an audit committee in operation throughout the financial year.                                | X |   |
|   | • The audit committee operates in accordance with approved, written terms of reference.                                       |   | X |
|   | • The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.    |   | X |
| 7.  | Internal audit  |   |   |
|   | • The district municipality had an internal audit function in operation throughout the financial year.                        |   | X |

| No.  | Matter   | Y | N |
|--|--|---|---|
|  | <ul style="list-style-type: none"> <li>The internal audit function operates in terms of an approved internal audit plan.</li> </ul>  |   | X |
|  | <ul style="list-style-type: none"> <li>The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.</li> </ul>   |   | X |
| 8.   | There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.  |   | X |
| 9.   | There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.  |   | X |
| 10.  | The information systems were appropriate to facilitate the preparation of the financial statements.  | X |   |
| 11.  | A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.   |   | X |
| 12.  | Powers and duties have been assigned as set out in section 79/106 of the MFMA.   |   | X |
| <b>Follow-up of audit findings</b>                                 |  |   |   |
| 13.  | The prior year audit findings have been substantially addressed.   |   | X |
| 14.  | SCOPA resolutions have been substantially implemented.   |   | X |
| <b>Issues relating to the reporting of performance information</b> |  |   |   |
| 15.  | The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.  |   | X |
| 16.  | Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.  |   | X |
| 17.  | A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the Thabo Mofutsanyana District Municipality against its mandate, predetermined objectives, outputs, indicators and targets section 68/87 of the MFMA. |   | X |
| 18.  | There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.  |   | X |

**Overall reflections on the governance framework based on other key governance requirements.**

60. Management responses to audit findings were not made in a timely manner as a result of the lack of availability of key staff members.
61. The financial statements were subject to a number of material corrections as a result of a consultants not being supplied with accurate and all relevant supporting documentation required.
62. Sufficient control measures were not developed by the accounting officer and chief financial officer, in conjunction with their support team, to address all the control and financial deficiencies as identified in prior years.
63. The chief financial officer did not attend any of the steering committee meetings and was not available to assist during the audit.

64. The audit committee was not able to execute their mandate effectively due to the internal audit department not supplying any audit reports in accordance with the internal audit plan. Appropriate steps had not been implemented to ensure that risk assessment is finalised and implemented during the current year. The fraud prevention plan as well as internal policies and procedures had not yet been compiled and implemented.
65. Policies and procedures related to financial reporting, risk management and compliance with laws and regulations were drafted during the current financial year and must still be approved and implemented.
66. The formal risk assessment was not completed due to it not being prioritised by management.
67. SCOPA resolutions were not substantially implemented due to these resolutions not being prioritised and addressed by management.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

### **Report on performance information**

68. I was engaged to review the performance information.

### **The accounting officer's responsibility for the performance information**

69. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

### **The Auditor-General's responsibility**

70. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
71. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
72. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

### **Findings on performance information**

#### **Non-compliance with regulatory requirements**

#### **No reporting of performance information**

73. The annual report of the Thabo Mofutsanyana District Municipality did not include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the MSA, as required by section 121(3)(c) of the MFMA.

#### **Content of integrated development plan**

74. The integrated development plan of the Thabo Mofutsanyana District Municipality did not include the key performance indicators and performance targets determined in terms of its performance management system, as required by sections 26(i) and 41(1)(b) of the MSA and regulation 12 of the Municipal Planning and Performance Management Regulations, 2001.
75. A copy of the IDP was not submitted to the MEC for Local Government within 10 days after the approval of the document as required by section 32 of the MSA.

#### **Existence and functioning of a performance audit committee**

76. The Thabo Mofutsanyana District Municipality did not appoint and budget for a performance audit committee, nor was another audit committee utilised as the performance audit committee, as required by regulation 14(2) of the Municipal Planning and Performance Management Regulations, 2001.

#### **Internal auditing of performance measurements**

77. The Thabo Mofutsanyana District Municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes, as required in terms of section 45 of the MSA.

#### **Lack of adoption or implementation of a performance management system**

78. The Thabo Mofutsanyana District Municipality did not adopt a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players, as required in terms of regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

#### **No mid-year budget and performance assessments**

79. The accounting officer of the Thabo Mofutsanyana District Municipality did not (by 25 January of each year) assess the performance of the municipality during the first half of the financial year, taking into account the municipality's service delivery performance during the first half of the financial year and the service delivery targets and performance indicators set in the service delivery and budget implementation plan, as required by section 72 of the MFMA.



## APPRECIATION

80. The assistance rendered by the staff of the Thabo Mofutsanyana District Municipality during the audit is sincerely appreciated.

*Auditor-General*

Bloemfontein

30 November 2009



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*